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EDUCATION, DEPARTMENT OF

A draft of the Audit Guide for Student Financial Aid Programs to be used for auditing the Department of Education's funded programs at colleges and universities has been issued by the Office of Inspector General of the Department of Education. Pending issuance of the final version, the draft guide is to be used as guidance in planning and performing preliminary work on audits for the period ending 6/30/83. The guide consolidates and streamlines two separate audit guides previously in use.

GENERAL ACCOUNTING OFFICE

Inadequate reporting to the IRS by over 28,000 tax exempt private foundations, representing over $35 billion in assets, has been charged by the U.S. General Accounting Office in recent testimony before a subcommittee of the House Committee on Government Operations. Johnny C. Finch, Associate Director, General Government Division, GAO, testified on IRS efforts to enforce tax exempt private foundation reporting requirements. Mr. Finch stated that the IRS code requires extensive reporting by these foundations and makes those returns available for public inspection. Mr. Finch said the "IRS has devoted little attention to certain reporting requirements for information which would be useful to the public and the Congress for monitoring foundation activities and to grant seekers for identifying those foundations most likely to fund their programs." He continued, "Consequently, most foundations do not comply well with those requirements." Mr. Finch then recommended a combined IRS enforcement approach with involves certain changes to the service center correspondence program and changes in the examination process itself.

SECURITIES AND EXCHANGE COMMISSION

Regulatory authorities should set stricter guidelines for auditors, according to comments by Theodore C. Focht, General Counsel, Securities Investor Protection Corporation (SIPC), before a SEC Major Issues Conference in Atlanta, GA. Speaking before a group which also heard from SEC Chairman John S.R. Shad, Mr. Focht stated that there were some major lessons to be learned form recent failures of stockbrokerage firms which resulted in losses to investors and which also resulted in payments to these same investors by SIPC. Citing the failure of one particular firm, Mr. Focht expressed surprise that the auditors did not detect the existance of a substantial number of bogus stock certificates. He went on to say that "our system depends on the job being done by public accountants." Mr. Focht also criticized regulatory authorities for not examining brokerage firm participants more closely and the firms themselves for not exercising more care about who is working in their firms. The SIPC insurance fund derives its revenue from a fractional assessment of brokerage firm revenues. Funds are then paid to investors who have sustained losses incurred in brokerage firm failures. Mr. Focht commented that recent SIPC proceedings have increased in number and have been the most expensive. He commented that the SIPC insurance fund has declined from $219 million in September 1981 to a current level of $141 million.

TREASURY, DEPARTMENT OF

Proposed regulations implementing the substantial underpayment tax penalty were critiqued during a panel discussion at the recent spring meeting of the AICPA Federal Tax Division in Washington, D.C. Panel members discussed the regulations proposed 3/10/83 (see the 3/14/83 Wash. Rpt.) and comments offered by the AICPA in response to the proposal. While agreeing that some aspects of the issue were successfully addressed by the proposal, the panel also felt that many taxpayers have "no real" guidance for dealing with the penalty in tax shelter and non-tax shelter situations. Copies of the AICPA's comments on the proposed regulations under Section 6661 (Penalty for Substantial Understatement of Tax) are available at 202/872-8190, ext. 47.

SPECIAL: BOTH CHAMBERS REINTRODUCE WORLDWIDE COMBINED REPORTING SYSTEM

Legislation to prohibit states from using the worldwide combined reporting system in taxing multinational corporations was reintroduced in both chambers of Congress recently. The bills would also conform state rules for taxing dividends received by domestic corporations from their overseas subsidiaries to the rules of the federal government in terms of the quality of the dividends which are taxed by the states. The Senate measure, S. 1225, was offered by Sen. Charles Mathias (R-MD), while Rep. Barber Conable (R-NY), the ranking minority member of the House Ways and Means Committee, was joined by eight other members of the tax writing panel in introducing H.R. 2918. For corporations doing business in more than one state, most states use the unitary method of tax assessment. Under this system, income subject to tax generally is computed on the ratio of payroll, sales, and property in the taxing state compared to all states. When extended to taxation of multinational, the method is called the worldwide combined reporting system. According to Sen. Mathias, "This has the effect of extending their tax tentacles overseas, contrary to federal policy, based on an arms length method, which treats affiliates and foreign subsidiaries in a corporate family as separate businesses for taxing purposes."

SPECIAL: PPSSCC RELEASES DRAFT REPORTS FOR GOVERNMENT SAVINGS

Six draft reports recommending $30 billion in potential cost savings for the Federal Government over a three year period have been released by the President's Private Sector Survey on Cost Control. The reports cover user charges, federal boards and commissions, banking regulation, federal land management, and the State Department. A set of recommendations for banking related agencies could save the government $9.4 billion over the three year period according to one of the reports. Changes which the panel said are most important would encourage quasi-governmental agencies to become private entities and would consolidate the regulatory and examination functions of the three bank regulators into one entity. The report continues by recommending that credit unions should no longer be exempt from taxes because they now function like other financial institutions and compete directly with banks and S&Ls. Other reports cover a wide range of business related agencies. Proposals include various methods for improving the competitiveness of the postal service, converting Federal Riot Insurance and Federal Crime Insurance into private companies, and a reduction in the general economic research of the FTC's Bureau of Economics.

SPECIAL: AICPA IS CRITICAL OF IRS POLICY OF DENYING ACCOUNTING METHOD CHANGE

The AICPA has recently criticized the IRS for abusing its discretion in denying accounting method changes for taxpayers requesting approval to switch from the accrual method to the cash method for tax purposes. In a 4/27/83 letter from AICPA Federal Tax Division Chairman William L. Raby to Assistant Treasury Secretary John E. Chapoton, which introduces a lengthy analysis of the subject, Chairman Raby said, "The Commissioner's (IRS) refusal to grant permission to change to the cash method for tax purposes based on a different clear reflection of income standard than the adoption of the cash method is inappropriate, improper and an abuse of his discretion." He also critiqued the problem by indicating that the IRS had recently, without notice, changed the unpublished criteria for changes from accrual to cash method accounting. The unpublished nature of the change, he said, "makes it impossible to determine the technical merit or policy basis upon which it was made." Complaining that "the service's current unpublished ruling policy results in an inequitable and arbitrary application of the law to similarly situated taxpayers," Chairman Raby indicated that while the Service is not granting changes to the cash method, new taxpayers may elect to use the cash method. As a result he said, "taxpayers in identical trades or businesses are subject to two different applications of the law." In an apparent response on the issue, IRS Associate Chief Counsel Gerald Portney indicated in remarks to the AICPA Accounts Division, 5/17/83, that the IRS will continue to deny most requests to change from accrual to cash method accounting. He further indicated that there may be an increase in the number of challenges against those businesses which initially adopt the cash method "because there is no absolute, incontrovertible right" for taxpayers who have adopted the cash method to remain on it.

SPECIAL: VOLKER OPPOSES INDEXING

Indexing tax rates to inflation is not a good idea, according to a recent letter from Federal Reserve Chairman Paul Volcher to Sen. Thomas Eagleton (D-MO). Mr. Volker suggests that indexing may tend to let the public and the government avoid facing up to inflation. "Indexing in general tries to evade the consequences of inflation, and we would be better advised to deal with the ailment directly." Mr. Volker rejects the argument that indexing will discourage government spending by stating, "I suspect that public concern with the effects of inflation in the presence of an unindexed tax system should serve to focus attention on the heart of the matter - discipline in both monetary and fiscal policies." He also suggests that indexing will contribute to rising future deficits and added that if Congress decides to keep indexing, "other measures of closing the deficit should be found." Mr. Eagleton has introduced a measure that would defer indexing until federal deficits are reduced to 2 percent or less of the gross national product, S. 1169.

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